United States Court of Appeals

for the Second Circuit

BRIEF FOR APPELLEE

76-6109

United States Court of Appeals

For the Second Circuit

Docket No. 76-6109

HUNTINGTON TOWERS, LTD. and
RICHARD CAREY,

Plaintiffs-Appellants,

against

FRANKLIN NATIONAL BANK (in liquidation),
FEDERAL DEPOSIT INSURANCE CORPORATION,

Defendants,

and

FEDERAL RESFRVE BANK OF NEW YORK,
EUROPEAN-AMERICAN BANK and JAMES SMITH,
individually and as Comptroller of the Currency,

Defendants-Appellees.

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F/S

BRIEF OF DEFENDANT-APPELLEE EUROPEAN-AMERICAN BANK & TRUST COMPANY

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BRIEF OF DEFENDANT-APPELLEE EUROPEAN-AMERICAN BANK & TRUST COMPANY

Issues Presented

1. Did the District Court err in holding that the New York statute of frauds bars plaintiffs' claim of an enforcible contract, when plaintiffs allege only that European-American Bank & Trust Company ("European-American") gave oral "assurances" of mortgage financing?

2. Did the District Court err in holding that a purchaser from the official receiver of an insolvent national

bank is entitled to protection from the bank's general liability, where the undisputed facts were that the purchaser paid fair value in a competitive bidding situation and that the receiver had statutory authority to enter into the transaction?

Statement of the Case

Status on Appeal

As against European-American, plaintiffs-appellants ("plaintiffs") apparently appeal only as to that portion of the District Court's holding which barred their claim on the basis of the New York statute of frauds. Plaintiffs in their brief have not resumed their argument that European-American is generally liable for the debts of the insolvent Franklin National Bank ("Franklin"). Plaintiffs have raised a new issue, however, that was not before the District Court—whether European-American had a contractual obligation to plaintiffs by virtue of its contract with Franklin's receiver, the Federal Deposit Insurance Corporation ("FDIC"), for the purchase of certain of Franklin's assets.[1]

Although plaintiffs have dropped the argument, a non-party to this litigation, Sol Neil Corbin (the trustee of the bankrupt Franklin New York Corporation—Franklin's holding company), has filed an amicus brief asking the Court to avoid deciding whether European-American is entitled to the protections afforded a bona fide purchaser. According to Mr. Corbin, resolution of the issue is not

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[1] Plaintiffs also appeal from dismissal of their separate claims against Federal Reserve Bank of New York and James Smith. Plaintiffs' appeal against Franklin National Bank in liquidation and FDIC was withdrawn by stipulation.

necessary for affirmance, and he wishes to avoid appellate precedent because he plans to pursue, in separate litigation, whether European-American exercised "due diligence" (Amicus Brief at 6) in consummating the transaction.

The District Court's holding that European-American is a bona fide purchaser was made only after full briefing of the issue by both sides, and was both necessary to disposition of the case and clearly correct. Since Mr. Corbin nowhere alleges that European-American purchased the assets other than in good faith, for value and at arms length, European-American submits that its status as a bona fide purchaser from the FDIC should be addressed by this Court and finally laid to rest. European-American relied on the FDIC's clear statutory authority to sell the assets, and paid fair value, and should not be compelled to relitigate continually whether it is generally liable for Franklin's debts.

Factual Background

Because of unusually large foreign exchange losses at Franklin, which were made public when discovered by regulatory authorities in May 1974, the Comptroller of the Currency and the FDIC in the summer of 1974 developed contingency plans for a possible sale of all or part of Franklin's assets. To that end, in late summer other commercial banks were contacted and, eventually, bids for portions of Franklin's assets were solicited. The Federal Reserve Bank, which had advanced almost $1.8 billion to Franklin while regulatory authorities were attempting to determine the best means to rectify the situation, on October 7, 1974 informed the Comptroller that continuation of the credit assistance was no longer in the public

interest and would be halted. The next day, the Comptroller declared Franklin insolvent and appointed the FDIC as receiver pursuant to 12 U.S.C. §§ 191 and 1821 (c). The FDIC, pursuant to 12 U.S.C. § 1823(c), then received bids from the four banks which had agreed to bid on Franklin's assets if it were declared insolvent, and, after approval by the District Court pursuant to 12 U.S.C. § 192, sold approximately one-half of Franklin's assets to European-American, which was the highest bidder. (JA 117-24, 164-69).

Under the Purchase and Assumption Agreement (JA 36-100) European-American assumed certain liabilities and offsetting assets, and agreed in addition to pay the receivership estate $125 million as a premium (JA 32). European-American did not assume the general liabilities of Franklin under the agreement (JA 33) and only had the right to accept approximately one-half of Franklin's assets. As to certain assets, including most of the mortgage loan portfolio, European-American had a certain time period in which to select the assets which would offset the liabilities it had assumed on October 8, 1974 (JA 54-56). Franklin's loans to plaintiffs were not among the assets chosen, and Franklin's receiver, the FDIC, retained the liens and notes which plaintiffs had given Franklin (JA 31-33, 168).

Subsequent to the Purchase and Assumption Agreement between the FDIC and European-American of October 8, but before European-American had been able to study the individual items in Franklin's loan portfolio in order to choose the loans it would assume, plaintiffs and one of their subcontractors exerted substantial pressure upon the FDIC and European-American to advance funds under threat of jeopardizing the entire investment.

On October 18, at a meeting between plaintiff Carey and two European-American officers, European-American loaned plaintiffs $100,000 on a thirty day note to enable plaintiffs to pay an antecedent obligation to their steel contractor, Ikenson Iron Works. Soon thereafter, European-American decided that financing of the project on a regular basis would not be prudent and it decided not to assume the liens and notes from the FDIC. Plaintiffs defaulted on the loan of $100,000. (JA 169-70).

Plaintiffs claim that at the October 18 meeting European-American gave "assurances" of financing (Complaint ¶ 14, JA 7) and list the factors by which they reached their "understanding" of the import of the discussion (Ikenson affidavit ¶ 11, JA 133; Carey Affidavit ¶ 4, JA 135-36). They refer to a memo dated October 17 (JA 156) between the two officers who had handled the account at Franklin to corroborate their assertions, although plaintiffs do not argue on appeal that this internal memorandum, which generally analyzes plaintiffs' project, constitutes an enforceable contract. The memo concludes with a discussion of the short-term alternatives; the two former Franklin officers agreed between themselves that in the "meantime", in order "to enable the continuance of the construction project", "it is important to provide funds."

Such funds were in fact provided at the meeting so that European-American and the FDIC could have the opportunity to make a reasoned decision as to this troubled property (JA 169-70, 157-58). Plaintiffs, who allege no extra expense on their part as a result of the meeting or the loan, do not deny that they benefited from the delay both financially and by the fair consideration given their project.

Plaintiffs' allegations that European-American officers gave "assurances" that "financing of construction by European-American or FDIC would continue" (Complaint ¶ 14, JA 7) are vigorously denied by European-American. But assuming the truth of all plaintiffs' allegations, such alleged "assurances" and proclamations of intent to help Long Island (JA 133, 136) do not constitute an agreement in any sense, much less an agreement valid and binding under the statute of frauds.

ARGUMENT

I.

The Statute of Frauds Bars Plaintiffs' First Claim

A. The Statute of Frauds Is Applicable to the Alleged Agreement

Before the District Court, plaintiffs acknowledged that mortgage loans by banks are subject to the provisions of the statute of frauds governing real property. General Obligations Law § 5-703(1) (23A McKinney 1964) (*see* JA 129).

On appeal, however, plaintiffs try to avoid application of the statute of frauds by reference to 12 U.S.C. § 371, a Federal statute governing the loan portfolios of national banks. This statute, however, merely embodies a legislative determination of prudence in the operation of a national bank. It limits, *inter alia,* the amount a national bank may lend to a fraction of the appraised value of the real estate securing the loan, and places an aggregate limit on loans which a national bank may make on real estate. In determining the amount of credit that may be extended, the statute provides that certain low-risk real

estate loans "shall not be considered real estate loans within the meaning of this section". 12 U.S.C. § 371(e).

These federal statutory controls on bank lending do not purport to define "real estate" and, in any event, are completely irrelevant to rules governing the writing necessary to constitute an enforceable contract on a real estate interest.[2] Moreover, European-American is not a national banking association and thereby subject to the provisions plaintiffs cite, but rather is chartered under the laws of the State of New York.[3] Whether European-American contractually obligated itself to plaintiffs is a matter of state law.

B. The Statute of Frauds Bars Enforcement of the Alleged "Assurances"

The purpose of the desired loan financing was for development of real property (JA 7).[4] In New York,

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[2] In New York mortgages can be considered personal property for some purposes but are considered real property for purposes of the Statute of Frauds. *Sleeth* v. *Sampson,* 237 N.Y. 69, 142 N.E. 355 (1923). *See United States* v. *General Douglas MacArthur Sr. Vil., Inc.,* 337 F. Supp. 955, 964-65 (E.D.N.Y. 1972). *See also Reconstruction Finance Corp.* v. *Beaver County, Pa.,* 328 U. S. 204, 210 (1946), where the Supreme Court indicated that, even while interpreting federal statutes, state rules defining real estate should be utilized unless they "patently run counter" to the federal regulation:

> "[T]he Congressional purpose can best be accomplished by application of settled state rules as to what constitutes 'real property' so long as . . . the state rules do not effect a discrimination against the Government, or patently run counter to the terms of the Act."

[3] Nor was European-American a member bank of the Federal Reserve System on October 18, 1974, when the alleged oral "assurances" were made. Even if it had been, it would not have been subject to the provision relied on by plaintiff, which, we reiterate, applies only to national banks. 12 U.S.C. § 330. *Compare* 12 U.S.C. 371 *with, e.g.,* 12 U.S.C. § 371b-1 *and* 12 U.S.C. § 371d.

[4] Plaintiffs sought financing for their construction project. Buildings are considered real estate, *e.g., Rosen* v. *Hummel,* 47 App. Div. 2d 782 (3d Dep't 1975).

agreements to transfer estates or interests in real property, to be enforceable, must be "in writing, subscribed by the person creating . . . the same, or by his lawful agent." General Obligations Law § 5-703(1) (23A McKinney 1964).[5] Plaintiffs admit that they have no note or memorandum evidencing a contract with European-American (JA 129).[6]

Mortgages and contracts to give mortgages are subject to the provisions of the statute of frauds. *Sleeth* v. *Sampson,* 237 N.Y. 69, 142 N.E. 355 (1923) (Cardozo, J.). Agreements to extend or modify mortgages or liens on real property are also subject to the statute of frauds. *Oneida Park, Inc.* v. *First National Credit Corp.,* 36 Misc. 2d 1085, 234 N.Y.S. 2d 168 (Sup. Ct. Onondaga 1962).

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[5] In full, § 5-703(1) reads:

"§ 5-703. *Conveyances and contracts concerning real property required to be in writing*

1. An estate or interest in real property, other than a lease for a term not exceeding one year, or any trust or power, over or concerning real property, or in any manner relating thereto, cannot be created, granted, assigned, surrendered or declared, unless by act or operation of law, or by a deed or conveyance in writing, subscribed by the person creating, granting, assigning, surrendering or declaring the same, or by his lawful agent, thereunto authorized by writing. But this subdivision does not affect the power of a testator in the disposition of his real property by will; nor prevent any trust from arising or being extinguished by implication or operation of law, nor any declaration of trust from being proved by a writing subscribed by the person declaring the same."

[6] As discussed above at page 5, before the District Court plaintiffs by supplementary affidavit sought to construe the memorandum of October 17 as an enforceable contract. As the memorandum never evidenced an intent to provide continued financing, or gave any of the terms of any such agreement, but was merely an internal discussion between two employees analyzing the present status of plaintiffs' project, the District Court rejected it as a contract. Plaintiffs on appeal have not resumed this argument.

In the same context as this case, *i.e.*, an alleged oral agreement to lend money on real property, the court in *Donahue* v. *Manufacturers Trust Co.*, 10 Misc. 2d 298, 300, 166 N.Y.S.2d 174, 177 (Sup. Ct. Westchester 1957) explained the reasons why the New York statute of frauds makes such agreements unenforceable:

> "The court cannot lose sight of the fact that the purpose of the statute is to prevent litigation over oral agreements in relation to real property, where the terms are always dependent upon the uncertainty and varying memory of witnesses. This evil was to be remedied by the reduction of the terms of the contract to writing, so that the parties might not misunderstand the particulars of the contract which they were making, and that perjury might not be invited to sustain a claim which never had any real existence."

This case well illustrates the rationale of the statute of frauds. Plaintiffs have submitted affidavits explaining the statements by which they deduced European-American had promised to provide all the financing necessary to complete their project. The most concrete statement in their support is made in ¶ 8 of the Ikenson affidavit (JA 133), where Mr. Jacobs of European-American is alleged to have said: "We intend to finance construction of the job because we have a commitment to Long Island. You will have all of the same people here. Nothing will change." Aside from other deficiencies in plaintiffs' allegations, European-American has made clear that its recollection is to the contrary (*see* JA 34-35). Since the purpose of the statute of frauds is to avoid invitations to

perjury and the "varying memory of witnesses," *id.*, these disputed oral assurances are precisely the sort of which the statute of frauds forbids enforcement.

Plaintiffs invoke equitable arguments of "part performance" in avoidance of the statute of frauds. But the statute of frauds is strictly applied in New York, and the "part performance" alleged here is European-American's "part performance", not plaintiffs'! Nor do plaintiffs allege any "contract," oral or otherwise—at most their allegations add up to a statement of intent. Only by turning the statute of frauds on its head can plaintiffs avoid its provisions.

(i) *There are no allegations of an agreement, even oral, sufficient to constitute an enforceable contract*

Accepting all plaintiffs' allegations as true, there was never an enforceable contract. For example, in ¶ 4 of Carey Affidavit (JA 135-36), Mr. Carey outlines the factors by which he deduced that financing would continue.[7] But neither this nor any of the other affidavits presents any of the supposed terms of the hypothetical contract—the interest rate, the terms of repayment, the security, the duration, the conditions for continued financing, etc., are all left to the imagination of the Court. *See* R. POWELL, THE LAW OF REAL PROPERTY, ¶ 441.1 (1976). Nor do plaintiffs allege that such terms existed or were even discussed. In no sense was this a contract, oral or otherwise.

Viewed liberally, plaintiffs' affidavits point only to an alleged statement of intent to finance the project. This is

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[7] Plaintiffs' Rule 9(g) Counterstatement to European-American incorporates at ¶ 3 the allegations of these affidavits (JA 129-30).

not a contract. In *Ginsberg Machine Co.* v. *J&H Label Processing Corp.*, 341 F.2d 825 (2d Cir. 1965), plaintiff sued defendant on an alleged oral agreement to give the plaintiff an exclusive right to sell certain machines. The statement made by defendant, assumed true for the motion to dismiss, was similar to that alleged here.

> " 'You can build a machine and as long as you build a machine you can have the exclusive agency, and as long as I am in the Electric Sealing label business I'll see to it that you have an exclusive on the selling of the label machines' ". *Id.* at 826.

The Court upheld the applicability of the New York statute of frauds to dismiss the claim, and also said that defendant's alleged assurances did not in any event constitute a contract:

> "[T]his supposed agreement is at most merely the outline of a working arrangement, not a contract specifically establishing the rights and obligations of the parties. Vagueness, indefiniteness and incompleteness are the earmarks of what the parties shook hands on . . . ." *Id.* at 828.

See also Rindge v. *Baker*, 57 N.Y. 209, 218 (1874); *Villano* v. *G&C Homes, Inc.*, 46 App. Div. 2d 907, 362 N.Y.S. 2d 198 (2d Dep't 1974); *28 Mott Street Co.* v. *Summit Import Corp.*, 59 Misc. 2d 459, 299 N.Y.S.2d 763 (Civ. Ct. N.Y. Co.), *rev'd on other grounds*, 308 N.Y.S. 2d 658 (App. T. 1st Dep't 1969). Each of the cases cited above required that all material terms of the contract be established before the court would invoke the doctrine of equitable estoppel to take the transfer of an interest in real property

out of the statute of frauds.[8] *E.g., 28 Mott Street Co.* v. *Summit Import Corp., supra* at 462, 299 N.Y.S.2d at 767-68: "Neither party has testified to a completed agreement, oral or written. Terms remained to be negotiated."

Plaintiffs here merely allege that there was an oral assurance or statement of intention. As there is no *contract*, oral or written, even alleged, the claim should be dismissed.

(ii) *Plaintiffs did not partly perform*

Assuming there was an oral agreement susceptible to enforcement, the statute of frauds still requires dismissal since there is neither part performance, unjust enrichment, nor any other unfairness that might justify invoking the Court's powers in equity. Plaintiffs have cited two nineteenth century cases to support their claim of "part performance," but each of those cases involved at least one crucial factor not here present—the plaintiff expended money in reliance on the defendant's representation.[9]

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[8] *Rindge* v. *Baker, supra* at 218, listed the prerequisites for equitable estoppel in these circumstances, including the requirement that the agreement be enforceable by the court, with sufficient evidence of all the material terms:

> "(1) The act of parole performance must be referable to the alleged agreement and no other. (2) They must be such as render it a fraud on the defendant, to take advantage of the contract not being in writing. (3) The agreement to which they refer must be such as in its own nature is enforceable by the court. (4) There must be proper evidence of the parole agreement."

[9] In *Sprague* v. *Cochran,* 144 N.Y. 104, 38 N.E. 1000 (1894), the lender had loaned funds to the respondent and received a defective mortgage instrument. The Court there said that the lender's expenditure of funds, and receipt of a lien, albeit a defective one, was sufficient performance to allow the court to enforce a vendor's lien.

In *Smith* v. *Smith,* 125 N.Y. 224, 26 N.E. 259 (1891), the plaintiff expended a substantial sum to erect a building on defend-

Although a primary issue in the District Court, plaintiffs never stated that the alleged oral promises by European-American caused them to spend one cent. Indeed, plaintiffs' incantations of "part performance" are not related to any "part performance" by plaintiffs subsequent to European-American's alleged "assurances," but to part performance by European-American, which relied to *its* detriment on plaintiffs' obligation to repay the $100,000 note.

Plaintiffs seek on appeal to confuse the issue by discussing their performance prior to European-American's involvement, and then by equating without analysis European-American's obligations with those of Franklin. But plaintiffs never alleged that European-American assumed plaintiffs' obligations from Franklin,[10] nor did they allege that their debt to Franklin for any other reason was owed to European-American. The only performance by plaintiffs relevant to this claim is performance induced by European-American, not plaintiffs' construction efforts in prior years, and no such performance is alleged.

Thus, plaintiff Carey in his affidavits nowhere alleged any part performance or other reliance to his detriment

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ant's property, in reliance on defendant's representations that the building would belong to plaintiff and would be freely alienable. The court held that plaintiff's reliance—the personal expenditure of significant sums of money—was performance enough to avoid the statute of frauds.

[10] As the District Court noted, "the Purchase and Assumption Agreement made plain that any advance to a Franklin customer by [European-American], if made within 180 days after the bank closing, did not prevent [European-American] from rejecting the loan (¶¶ 3.5 and 3.6, pp. 17-21)" (JA 188).

as a result of European-American's alleged assurances.[11] Mr. Ikenson, who is not a party, alleges in his affidavit that he relied upon "that understanding" and continued his "erection project" for "a short time" (JA 133-34). Mr. Ikenson's supposed reliance is not in issue, however, and he certainly does not allege that he continued the project to an expense of $100,000, the amount he received from the European-American loan. It is unclear exactly how the doctrine of part performance can be utilized in the situation where the plaintiffs can swear to no loss. Even if some reliance on their part were hypothesized, plaintiffs presumably improved the structure which they owned, not one owned by European-American. Plaintiffs certainly made no expenditures for the benefit or to the profit of European-American, which made a substantial payment and received nothing in return. *See Rindge* v. *Baker*, note 8 *supra*.

New York case law is clear that the statute of frauds can be avoided by part performance only in the most clear situation of injustice, and only where plaintiffs' performance (if any) was "unequivocally referable" to the alleged oral contract. In *Wilson* v. *La Van*, 22 N.Y. 2d 131, 238 N.E.2d 738, 291 N.Y.S.2d 344 (1968), the plaintiffs and defendants reached an oral agreement to convey property; plaintiffs were to take possession of the property, maintain the building, pay the taxes and make the mortgage payments, and upon completion of the mortgage payments, defendants would convey the property to them. Plaintiffs remained on the property for 14 years, meeting

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[11] In ¶ 5 of his supplemental affidavit (JA 140), Mr. Carey alleges "plaintiffs then did find it necessary to draw as best as they could on other sources and did so in reliance upon FDIC's assurance that the financing would be forthcoming". As presented by plaintiffs, this "reliance" is not connected to European-American.

all the conditions, and upon defendants' breach, sued to compel the conveyance. Relying on the statute of frauds, the Court rejected their suit, holding that the part performance was not "'unequivocally referable' to an agreement to convey", since the facts as alleged were conceivably consistent with a landlord-tenant relationship. *Id.* at 134, 238 N.E.2d at 740, 291 N.Y.S.2d at 347.

In the instant case, plaintiffs' improvement of their own building is not "unequivocally referable" to any agreement or promise by European-American;[12] completion of plaintiffs' building was presumably in their self-interest.

Furthermore, New York courts uniformly require not merely "unequivocally referable" part performance, but also substantial performance, to the detriment of plaintiff and the benefit of defendant, to avoid the statute of frauds:

> "Like all acts of part performance, the improvements must be such as would not have been made except in reliance on the contract. They must be substantial and permanent in character and the loss thereof a sacrifice to the purchaser."

Cooley v. *Lobdell,* 153 N.Y. 596, 602, 47 N.E. 783, 784 (1897); *see also Moulton* v. *Moore,* 33 App. Div. 2d 887, 307 N.Y.S.2d 562 (4th Dep't 1969).

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[12] Similarly, European-American's advance of $100,000 is consistent with a single loan; it is also consistent with a decision by European-American to give itself time to decide whether or not it wanted to expand further financing. The existence of the loan hardly mandates a conclusion of a long-term contractual commitment to plaintiffs. In all events the "part performance" required to overcome the statute of frauds is "part performance" by the plaintiff, not the defendant.

In sum, there is not part performance sufficient to avoid the statute of frauds of New York where (1) plaintiffs do not allege reliance on the alleged assurances or specify any detriment; (2) plaintiffs' improvements, if any, were made on their own property; (3) such improvements are not "unequivocally referable" to the alleged assurances; and (4) European-American is not unjustly enriched.

II.

European-American Owed No Duty to Plaintiffs by Virtue of the Purchase and Assumption Agreement Between the FDIC and European-American. Nor Has European-American Breached Any Provision of that Agreement.

Plaintiffs in their complaint alleged that regulatory agencies acted unlawfully in connection with the declaration of Franklin's insolvency and that European-American orally "assured" plaintiffs of financing. Nowhere in the complaint is there the theory, presented for the first time on appeal, that European-American had contractural duties to plaintiffs arising out of the Purchase and Assumption Agreement between FDIC and European-American. That issue is thus not properly before this Court.

Plaintiffs' new theory is that because "this was a major construction project", European-American "had a duty to service the loan or immediately reject it" (Brief at 20). Aside from the impracticality of immediacy, as European-American was faced with making decisions as to over $3 billion in assets, European-American's duties under the

Agreement were only to service loans in accordance with "normal and prudent banking practices" (§ 3.7, JA 62). In § 3.6(f), the Agreement specifically contemplates that advances will not be given for sub-standard loans (JA 60-61). The purpose of §§ 3.6 and 3.7 of the Agreement, providing for the servicing of loans until reasoned decisions could be made on their disposition, was to preserve the viability of acceptable loan accounts for the benefit of the receivership estate.

European-American had the discretion to act "prudently" in making advances and decided not to continue Franklin's advances on the loan to plaintiffs' construction project.[13] Franklin's receiver, the FDIC, for whose ultimate account any such advances under the Agreement would have been made, agreed with European-American's decision and did not itself fund the loan. The FDIC's ultimate decision fully vindicated European-American's judgment that the project was not viable and that good money should not be thrown after bad. Other lending institutions apparently also agreed with this conclusion, assuming that plaintiffs made an effort to secure financing elsewhere.

But irrespective of whether European-American acted prudently, the simple fact is that the Purchase and Assumption Agreement conferred no rights on plaintiffs and imposed no duties upon European-American for their benefit.

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[13] The separate loan of $100,000 was made for European-American's own account in the confusion immediately after the takeover in order to ward off plaintiffs' creditors so as to afford time for a decision as to further advances. It proved to be an expensive act for European-American, since plaintiffs have made no effort to repay the note. Plaintiffs, on the other hand, gained not only economically but also by the fair consideration given their project.

III.

European-American Is Not Liable for Franklin's Debts.

Plaintiffs on appeal have not briefed their claim of illegality of the takeover transaction as to European-American. The undisputed facts are that European-American, relying upon the clear statutory authority given the FDIC to act as receiver and to dispose of the assets of Franklin, and pursuant to judicial confirmation of the same, 381 F. Supp. 1390 (E.D.N.Y. 1974), in a competitive bidding situation paid value for certain of Franklin assets. Nor was there any allegation in the complaint or in plaintiffs' affidavits that European-American acted other than in good faith, and the record is to the contrary.[14] In short, Judge Judd's conclusion that European-American was entitled to the protections afforded a bona fide purchaser, a finding also reached by the only other court to address the issue,[15] is unimpeachable.

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[14] Plaintiffs' general allegations of fraud in their complaint (¶ 21, JA 9), while arguably properly pleaded as to the other defendants through ¶¶ 6 and 7 as incorporated in ¶ 18 of the complaint, included no specific allegation as to European-American, and clearly did not meet the particularity of pleading requirements of F.R. Civ. P. 9(b). *See e.g., Siegel* v. *Gordon,* 467 F.2d 602, 607 (2d Cir. 1972); *Goodall* v. *Columbia Ventures, Inc.,* 374 F.Supp. 1324, 1333 (S.D.N.Y. 1974). Nor did plaintiffs, after joining of the issue, produce any evidentiary support or further allegations that might have tended to contradict the undisputed facts concerning European-American's role in the takeover—that it paid value in a competitive bidding situation and in reliance on the FDIC's statutory authority to enter into the transaction (JA 31-33).

[15] In *Varghese* v. *FDIC*, 75 Civ. 1831 (S.D.N.Y. 1975), Judge Lasker refused to allow plaintiff to join European-American, holding that, "[a]bsent an agreement to assume a specific liability, a purchaser from a receiver of bankrupt's assets does not assume the debts of the bankrupt." (Mem. opinion at 2). Judge Lasker pointed out that any judgment against a bank is binding upon the receiver, citing *Kaplan* v. *Joseph,* 125 F.2d 602, 606 (7th Cir. 1942), and concluded that the plaintiff "cannot recover any judgment against European-American on the basis of Franklin's alleged discrimination." *Id.*

Because of the necessary policy in favor of the finality of sales in bankruptcy, purchasers from receivers are generally immune from liability even if the sale by the receiver is wrongful. *See, e.g., In re Strunks Lane & Jellico Mountain Coal & Coke Co.*, 64 F. Supp. 731, 733 (E.D. Ky. 1946); *In re Rapier Sugar Feed Co.*, 13 F. Supp. 85, 88-89 (W.D. Ky. 1935). If a sale is in fact wrongful, the proper recourse, absent fraud by the purchaser or a defect in title, neither here properly alleged, is an action for damages against the receiver.[16] *See Schy* v. *Franklin National Bank*, 72 Civ. 718 (E.D.N.Y., March 3, 1975); *cf. In re Solantikas*, 29 F.2d 431 (W.D. Pa. 1928).

The same immunity is given to purchasers of trust property.[17] If a trustee has a general power to alienate trust property, it is clear that the beneficiaries of a trust

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[16] *See International Westminister Bank, Ltd.* v. *FDIC*, 509 F.2d 641, at 644 n.5 (9th Cir. 1975), where the court suggests that such a claim against the FDIC should be made under the Federal Tort Claims Act. In *International Westminister*, plaintiff creditors claimed, as in this case, that the manner in which the FDIC as receiver sold an insolvent bank's assets violated the FDIC's duty to creditors. The district court had dismissed the action for failure to state a claim upon which relief could be granted. The Ninth Circuit agreed with the District Judge on all but his denial to plaintiffs of an opportunity to replead and reversed to allow a new complaint.

See also The Regional Rail Reorganization Act Cases, 419 U.S. 102 (1974), where plaintiffs claimed that the operation of a statute, providing for transfer of the properties of bankrupt railroads, worked an unconstitutional deprivation of their property rights, and the Supreme Court upheld the validity of the statute, saying that the deprivation could be cured by an action by plaintiffs in the Court of Claims.

Thus, if plaintiffs have indeed been wronged, adequate recourse is available to them at the proper time in the proper forum, as recognized by the District Court below in refusing to dismiss the claims as to the FDIC.

[17] The receiver of a national bank can be described as a trustee for creditors. *E.g., Davis* v. *Knipp*, 92 Hun. 297, 36 N.Y.S. 705 (4th Dep't 1895).

cannot maintain any action against a bona fide purchaser of the property from a trustee, even if the trustee breached his fiduciary duty in selling the property. *See, e.g., Love* v. *Fauquet,* 184 Neb. 250, 166 N.W.2d 742 (1969); *Dodge* v. *Stone,* 76 R.I. 318, 69 A.2d 632 (1949); RESTATEMENT (SECOND) OF TRUSTS § 297, comment L (1959).

There is a clear and well-founded body of law which favors the finality of sales to bona fide purchasers, and which makes judicial sales virtually unimpeachable as regards the purchaser. Here, a federal statute expressly authorized the sale by the FDIC, and the policies of the statute were fully served by European-American's purchase. In a situation where, without the statutory procedure, there would have been enormous economic dislocation and where confidence in the Nation's financial institutions would have been badly shaken, the receivership of Franklin marked the end, not the beginning, of an unhappy saga in banking history. These are not the circumstances for making precedent which would discourage future purchases of an insolvent bank's assets.

Mr. Corbin's Amicus Brief

The trustee of Franklin New York Corporation has filed a brief asking this Court not to reach the issue of whether European-American is a bona fide purchaser. But Mr. Corbin's arguments in avoidance of appellate precedent raise no factual issues which might affect the validity of the holding below.

Mr. Corbin's complaint (Exhibit A to the affidavit of Michael O. Finkelstein) contains no allegation that European-American acted other than in good faith or paid less than fair value. Mr. Corbin complains of a fraud by

Franklin in April and May of 1974 in procuring a $30 million loan from Manufacturers Hanover Trust Co. ("Manufacturers"). Franklin New York Corporation, which apparently transferred the funds to Franklin, alleges that the transfer was induced by a fraud by Franklin. Mr. Corbin deduces that the proceeds of the loan eventually ended up in Franklin's receivership estate and may then have been transferred to the FDIC in its corporate capacity, to European-American, or to the Federal Reserve Bank. Assuming that this theory is correct, there is no allegation that European-American did not pay Franklin's receiver dollar for dollar for the assets it purchased, whatever their origin, or otherwise acted in bad faith in the transaction. Thus, Mr. Corbin's allegations of wrongdoing against Franklin have no bearing on the determination of European-American as a bona fide purchaser.

Mr. Corbin is of course the trustee of the party which defrauded Manufacturers, if anyone did, and his claim is derivative of Manufacturers'.[18] But after its loan was in default and the alleged fraud uncovered, Manufacturers vigorously competed with European-American to purchase Franklin's assets from the FDIC! In effect, Mr. Corbin is suggesting that Manufacturers, as well as European-American, should not have submitted a bid on Franklin, although federal banking laws were enacted precisely to facilitate such transactions.

The specific "legal arguments" which Mr. Corbin says he wishes to raise in his case are similarly without merit.

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[18] Manufacturers has itself sued the receivership estate of Franklin New York Corporation (for which Mr. Corbin is trustee) as well as the FDIC, the Federal Reserve Board and European-American on a "constructive trustee" theory. Manufacturers does not allege that European-American acted in bad faith or paid less than fair value.

He first argues that it was clearly incorrect to afford European-American protection as a bona fide purchaser since plaintiffs' claim was not dismissed as to the FDIC, and since the FDIC in its corporate capacity and European-American "were identically situated as transferees of FNB's assets" (Amicus Brief at 4). Certainly both European-American and FDIC were "transferees" of portions of Franklin's assets; but the pertinent issue is the circumstances under which the transfers were effected. European-American is a third party which purchased assets for value in an arms-length competitive bidding situation; the FDIC in its corporate capacity purchased certain assets and assumed certain obligations from the FDIC as receiver in a non-competitive transaction (as authorized by 12 U.S.C. § 1823). Insofar as the traditional criteria applicable to bona fide purchasers, the differences between the two transactions are substantial. One was at arm's length, between unrelated parties; the other was not.

Mr. Corbin then argues that Judge Judd erred in dismissing the claim against European-American "by reason of the FDIC's indemnity" of European-American with respect to Franklin liabilities not specifically assumed by European-American (Amicus Brief at 5). Contrary to Mr. Corbin's assertion, the District Court did not base its holding on the existence of the indemnity agreement; rather, the Court mentioned the indemnity agreement as an additional and very practical reason why European-American should not be a party to these cases (*see* JA 188-89).

Mr. Corbin apparently desires to make European-American a party to his action in order to avoid the limited sovereign immunity status that the District Court granted the FDIC in its corporate capacity (whereby dam-

ages claims are confined to the receivership estate, although restitutionary claims may be pursued to the FDIC in its corporate capacity). *See* Amicus Brief at 4-5. Mr. Corbin's attempt to thus circumlocute established law on sovereign immunity by tagging liability on the FDIC through European-American is hardly a compelling reason to avoid affirming the holding that European-American is a bona fide purchaser.

Lastly, Mr. Corbin falls back on the "issue" that the parties in this case "wholly failed to consider the question whether EAB had used 'due diligence' to determine the validity of the transaction so as to create immunity from claims." As "due diligence" is a term of art under § 11 of the Securities Act of 1933 and involving the issuance of securities it would seem that the parties below, concerned with the insolvency of a national bank and the sale of its assets by the FDIC, properly ignored the body of law governing registration of public offerings of stock. If Mr. Corbin means that European-American might have been negligent somehow by not realizing that Franklin New York Corporation had misrepresented to Manufacturers the state of Franklin National Bank's health, it is difficult to see any relevance to the point—European-American had nothing to do with that transaction, and no one has suggested or could suggest that European-American did not pay the FDIC value for whatever assets European-American received. Even if the $30 million were in "marked bills" and therefore somehow traceable, Mr. Corbin's claim is against Franklin, through its receiver, not against European-American. *See* notes 15 and 16, *supra*.

Aside from the lack of merit of his specific arguments, Mr. Corbin's theories should be rejected because they sig-

nificantly undermine the public policies embodied in the federal banking laws. Irrespective of the plethora of claims that might arise against the receiver of an insolvent bank, and irrespective even of those alleging fraud or unlawful preferences, the practical ability of the FDIC to follow the express Congressional mandate for continuance of banking services upon a bank's insolvency would be eliminated if a purchaser for value of the bank's assets thereby subjected itself to countless claims and years of litigation. The FDIC's ability to serve the vital public interest in avoiding the abrupt closing of a major money center bank cannot be made dependent upon whether or not the failing bank has committed a tort, or many torts, prior to its receivership.

CONCLUSION

For the reasons stated, the judgment of the District Court should be affirmed.

Respectfully submitted,

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Of Counsel

December 1, 1976

UNITED STATES COURT OF APPEALS

FOR THE SECOND CIRCUIT

- x

HUNTINGTON TOWERS, LTD. and RICHARD CAREY, :

Plaintiffs-Appellants, :

-against- :

FRANKLIN NATIONAL BANK (in liquidation) and FEDERAL DEPOSIT INSURANCE CORPORATION, : Docket No. 76-6109

:

Defendants,

:

FEDERAL RESERVE BANK OF NEW YORK, EUROPEAN-AMERICAN BANK and JAMES SMITH, individually and as a Comptroller of the Currency, :

:

Defendants-Appellees.

- x

STATE OF NEW YORK)
: SS.:
COUNTY OF NEW YORK)

GEORGE A. SCHOLZE, being duly sworn, deposes and says that he is an attorney associated with Sullivan & Cromwell, attorneys for European-American Bank; that on the 1st day of December, 1976 he caused the within brief to be served upon the following attorneys at the following addresses by having two true copies of the same delivered to each of the said attorneys at said addresses, by leaving the same with a person in charge of each office, as follows:

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Sworn to before me this
1st day of December, 1976

Alan Ihne

Notary Public

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Kings Co. Clk's No. 24-7031350
Certificate Filed in
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Commission Expires March 30, 1978